FDIC State Profile

Spring 2005

Texas

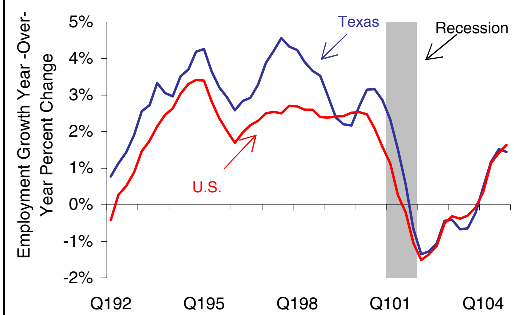
Texas employment growth is gathering momentum.

- Texas employment growth was still lagging behind the nation as of year-end 2004, a pattern that has held for the past two years (See Chart 1). With job growth picking up moderately, the state should establish a new quarterly employment peak sometime in the first half of 2005.
- At the end of 2004, construction and manufacturing are the only two major employment sectors in Texas still losing jobs, respectively at -1.1 and -0.04 percent. All remaining sectors are reporting positive growth.
- The **Laredo** MSA ranked fourth in the nation for employment growth in fourth quarter 2004. Laredo is benefiting from the growth advantages of cross-border trade with Mexico. However, the recent escalation in kidnappings and other crime in Mexico's border cities has prompted the U.S. State Department to issue a travel advisory which may, in the short run, affect the pace of economic growth in Laredo.

Budget cuts leave agricultural lenders and producers with worries.

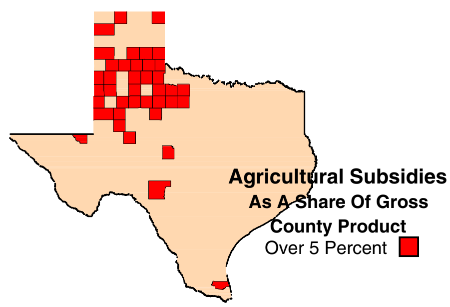
- The proposed 2006 federal budget would result in a reduction in USDA spending of 9.6 percent—at least $587 million next year and $5.7 billion over the next 10 years.[1]
- These cuts will disproportionately affect Texas because of the concentration of cotton production in the Texas High Plains Region, the capital intensive nature of cotton production, and the tendency for these farms to receive large subsidy payments. The counties in Texas with a large dependency [2] on agricultural subsidies are illustrated geographically (See Map 1).

Chart 1: 2004 Job Numbers Show Texas Employment Growth Slightly Trailing the Nation



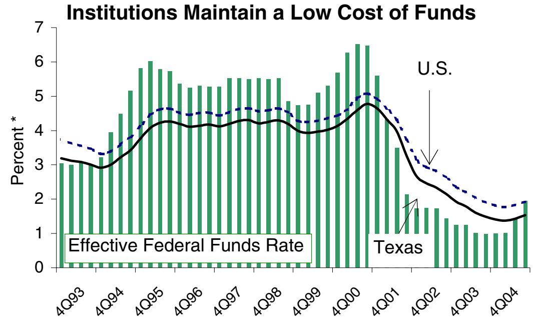
Source: BLS/Haver Analytics

Map 1: Highly Subsidized Counties Concentrated in Texas Panhandle and High Plains Area



Source: USDA, Economy.com and author's calculations

Chart 2: Noninterest Deposits Help Texas Institutions Maintain a Low Cost of Funds



*Note: Cost of funds is median quarterly annualized interest expense to average interest-bearing liabilities. The effective Federal Funds Rate is annualized based on a 360 day year.
Source: FDIC and Federal Reserve, Bank and Thrift Call Reports.

[1] Reynolds, John "Bush budget plan puts farm aid on chopping block," Lubbock Online.com, February 5, 2005.

[2] The average share of a county's gross product (CDP) from agricultural subsidies is well below 1 percent (0.18). For our analysis, a "large dependency" is a county where subsidies exceed 5 percent of CDP.

Lack of water availability could dampen future growth.

- The Texas High Plains section of the Ogallala Aquifer has long been a major source of water for agricultural, municipal, and industrial development.
- Texas' water plan predicts that by 2050 groundwater depletion will cause water supplied by the aquifer to decline by 24 percent. As water resources deplete, West Texas and the Northern High Plains area will be challenged.
- Water for the **San Antonio** Metropolitan Area is provided by the Edwards Aquifer. With the start of long term droughts in 2000, the aquifer level has dropped and could constrain economic growth in the San Antonio area.

Crude oil prices remain volatile.

- Crude oil prices continued their volatility. In March 2005, the price per barrel surpassed $56 (West Texas Intermediate crude), establishing a new all time high, supported by colder weather and concerns over tighter crude oil supplies.
- Oil prices in the first two months of 2005 were one-third higher from the same period a year ago.
- Although a select few industries (e.g. oil extraction and support services for mining) and geographical areas (e.g. **Houston**, the Gulf Coast and West Texas) stand to benefit slightly from higher crude prices, higher energy costs are expected to be a drag on the rest of the state's economy.

Texas insured institutions post exceptional results for 2004.

- Bank profitability and credit quality continue to post strong results. Texas headquartered banks and thrifts posted the highest annual average return on assets in the past ten years. Likewise, past-due and charge off rates are at decade lows.
- Contributing factors, including lower provision expenses, higher noninterest income, and security gains, likely will be difficult to sustain in future quarters. A longer term trend of compressing interest margins abated in the fourth quarter, but a changing interest rate environment and strong competitive factors, particularly in the large metro markets, will likely keep this an ongoing challenge. The performance gap between larger institutions and community banks continues to widen.[3]

Texas institution funding costs remain among the lowest in the nation.

- The median cost of funds for Texas insured institutions was 1.53 for the fourth quarter of 2004, ranking fifth lowest nationwide (See Chart 2). Texas institutions tend to hold higher levels of noninterest bearing deposits. Additionally, more than half of the state's insured institutions reside in rural areas, which often have fewer market competitors and provide bankers with greater influence in determining interest rates for both loan and deposit products.

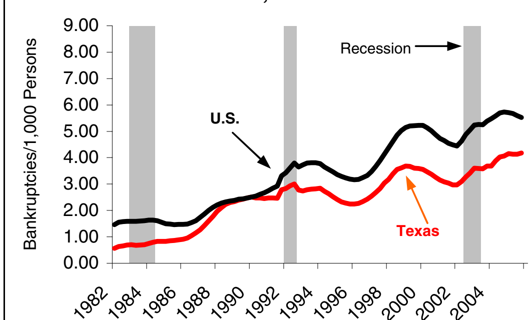
Consumer fundamentals show mixed results.

- Albeit below the national average, Texas per capita bankruptcy rates remain at record levels suggesting that the consumer sector is still vulnerable (See Chart 3). Additionally, single family mortgage foreclosures have shown modest improvement recently, but remain in the past decade's upper range.
- Combining these factors with low savings rates suggests that the consumer is still vulnerable to rising interest rates.
- Despite mixed results for consumer fundamentals, bank consumer past-due and charge off rates remain near decade lows speaking well to the ability of bankers to manage risk.

Home equity lines of credit (HELOC) continue to show impressive growth.

- Since HELOCs have only been available in Texas since 2003, the median concentration (HELOC to tier 1 capital) is among the lowest in the nation. However, Texas insured institutions doubled the dollar amount of HELOCs in 2004, suggesting this loan type could be a growth area moving forward.

Chart 3: Texas Per Capita Bankruptcy Rates Remain at Elevated Levels, Albeit Below the US



Note: Four quarter moving total.
Source: Administrative Office of the U.S Courts/Haver Analytics

[3]Community banks are defined as insured institutions with less than $1 billion in assets excluding credit card and specialty banks.

Texas at a Glance

ECONOMIC INDICATORS (Change from year ago quarter, unless noted)

Employment Growth Rates	Q4-04	Q4-03	Q4-02	Q4-01	Q4-00
Total Nonfarm (share of trailing four quarter employment in parentheses)	1.5%	-0.2%	-0.4%	-0.7%	2.8%
Manufacturing (9%)	0.0%	-4.2%	-6.4%	-7.2%	0.5%
Other (non-manufacturing) Goods-Producing (7%)	0.0%	-1.1%	-3.4%	1.6%	4.3%
Private Service-Producing (66%)	1.8%	0.5%	0.1%	-0.7%	3.4%
Government (17%)	1.4%	-0.3%	2.6%	2.6%	1.4%
Unemployment Rate (% of labor force)	5.9	6.6	6.5	5.7	4.3

Other Indicators	Q4-04	Q4-03	Q4-02	Q4-01	Q4-00
Personal Income	N/A	4.8%	0.7%	2.7%	8.5%
Single-Family Home Permits	5.7%	7.5%	14.0%	1.4%	13.3%
Multifamily Building Permits	-21.2%	-12.2%	-3.0%	65.6%	-38.2%
Existing Home Sales	10.6%	10.4%	6.2%	3.5%	3.6%
Home Price Index	3.8%	2.5%	3.9%	6.2%	5.8%
Bankruptcy Filings per 1000 people (quarterly level)	1.01	1.03	0.94	0.94	0.76

BANKING TRENDS

General Information	Q4-04	Q4-03	Q4-02	Q4-01	Q4-00
Institutions (#)	681	697	715	735	759
Total Assets (in millions)	215,442	200,187	216,906	199,340	233,380
New Institutions (# < 3 years)	24	20	16	20	27
Subchapter S Institutions	263	259	250	228	200

Asset Quality	Q4-04	Q4-03	Q4-02	Q4-01	Q4-00
Past-Due and Nonaccrual Loans / Total Loans (median %)	1.77	2.04	2.24	2.19	2.04
ALLL/Total Loans (median %)	1.23	1.27	1.25	1.21	1.18
ALLL/Noncurrent Loans (median multiple)	2.14	1.91	1.71	1.84	2.04
Net Loan Losses / Total Loans (median %)	0.14	0.19	0.23	0.19	0.15

Capital / Earnings	Q4-04	Q4-03	Q4-02	Q4-01	Q4-00
Tier 1 Leverage (median %)	9.42	9.07	8.96	8.81	9.06
Return on Assets (median %)	1.05	1.03	1.10	1.07	1.21
Pretax Return on Assets (median %)	1.34	1.29	1.40	1.39	1.64
Net Interest Margin (median %)	4.24	4.23	4.49	4.46	4.76
Yield on Earning Assets (median %)	5.44	5.60	6.37	7.62	8.30
Cost of Funding Earning Assets (median %)	1.10	1.33	1.90	3.16	3.51
Provisions to Avg. Assets (median %)	0.12	0.16	0.20	0.17	0.16
Noninterest Income to Avg. Assets (median %)	0.92	0.93	0.89	0.90	0.89
Overhead to Avg. Assets (median %)	3.42	3.37	3.42	3.42	3.49

Liquidity / Sensitivity	Q4-04	Q4-03	Q4-02	Q4-01	Q4-00
Loans to Assets (median %)	56.7	53.8	54.7	54.3	54.6
Noncore Funding to Assets (median %)	16.8	16.3	16.5	16.5	15.9
Long-term Assets to Assets (median %, call filers)	13.3	13.6	12.1	12.6	11.3
Brokered Deposits (number of institutions)	78	76	57	49	46
Brokered Deposits to Assets (median % for those above)	3.4	2.8	3.3	1.9	2.0

Loan Concentrations (median % of Tier 1 Capital)	Q4-04	Q4-03	Q4-02	Q4-01	Q4-00
Commercial and Industrial	84.6	85.8	90.1	93.6	92.2
Commercial Real Estate	152.7	144.8	134.0	123.6	111.7
Construction & Development	26.9	26.5	23.5	21.0	18.5
Multifamily Residential Real Estate	1.8	2.0	1.8	1.7	1.7
Nonresidential Real Estate	106.9	98.4	92.6	88.1	82.2
Residential Real Estate	99.5	102.8	107.1	107.3	105.0
Consumer	64.6	70.9	78.1	88.4	96.4
Agriculture	37.6	35.7	36.3	35.1	33.1

BANKING PROFILE

Largest Deposit Markets	Institutions in Market	Deposits ($ millions)
Dallas-Fort Worth-Arlington, TX	165	93,060
Houston-Baytown-Sugar Land, TX	107	83,930
San Antonio, TX	60	27,962
Austin-Round Rock, TX	61	13,841
McAllen-Edinburg-Pharr, TX	17	6,350

Asset Distribution	Institutions
< $250 mil.	564 (82.8%)
$250 mil. to $1 bil.	86 (12.6%)
$1 bil. to $10 bil.	28 (4.1%)
> $10 bil.	3 (0.4%)